EX PARTE OR LATE FILED

Southwestern Bell

July 20, 1994

Stephen S. Melnikoff
Vice President
Federal Regulatory

Ex Parte

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, N.W., Room 222
Washington, D.C. 20554

Re: MFS Petition for Rulemaking RM-8480

Dear Mr. Caton:

Attached is the material provided to the Commission during the ex parte meeting mentioned above, and which was not available when Southwestern Bell filed its ex parte notification dated July 18, 1994. With this submission, all material provided at the meeting has been filed.

Sincerely,

Stephen S. Melnikoff

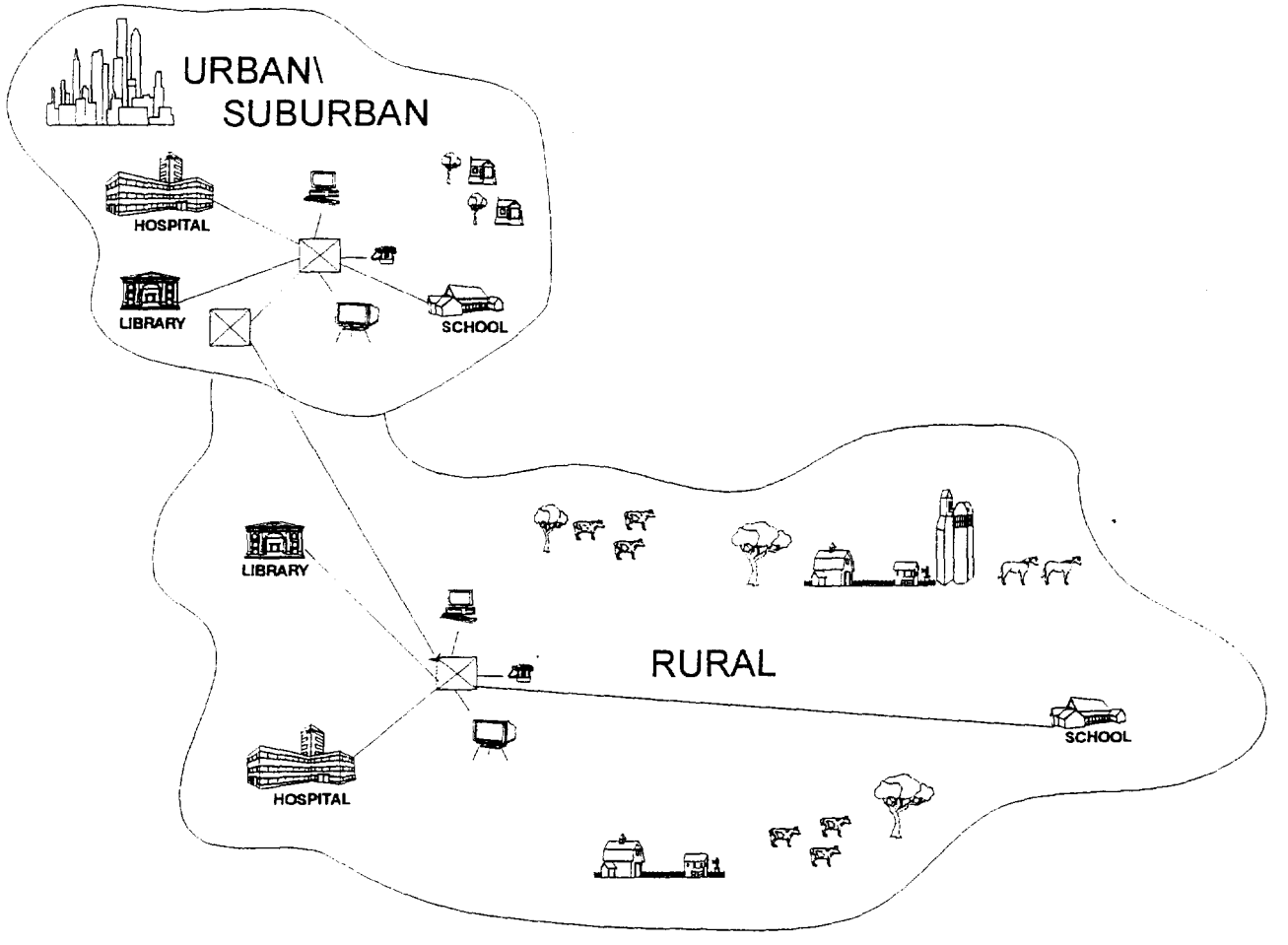
Attachment
cc: Suzanne Tetreault
Mark Nadel
Larry Povich

1401 I Street, N.W.
Suite 1100
Washington, D.C. 20005

Phone 202 326-8885

UNIVERSAL SERVICE:

YESTERDAY, TODAY, AND TOMORROW



UNIVERSAL SERVICE INDEX

UNIVERSAL SERVICE INDEX

UNIVERSAL SERVICE:

AN EXECUTIVE SUMMARY

SOUTHWESTERN BELL TELEPHONE COMPANY

Universal Service

Introduction

Universal Service is a topic that is currently receiving much attention within the telecommunications industry, regulatory bodies, legislative forums, and the Clinton Administration. This paper provides a Southwestern Bell Telephone Company (SWBT) viewpoint on a number of issues related to Universal Service, including: a) Definition; b) Carrier of Last Resort; c) Support Mechanisms; d) Cost Recovery, and e) Use of a Voucher System. This paper also addresses some of the initiatives undertaken by other parties, including the current activities of the National Association of Regulatory Utility Commissioners (NARUC).

Definition

Within the telecommunications industry, a large amount of work is being done in connection with Universal Service policy issues. One of the first issues being discussed is a definition of Universal Service. The concept of Universal Service manifests itself in the Communications Act which specifies that the Federal Communications Commission (FCC) was created "... to make available, so far as possible, to all people of the United States a rapid, efficient, Nation-wide, and world-wide wire and radio communication service with adequate facilities at reasonable charges, for the purpose of the national defense," and "promoting safety of life and property" (Communications Act of 1934, as Amended, Section 1, [47 U.S.C. § 151]). Thus, **Universal Service is the conceptual goal of making communications service available to all people in the United States, which has been translated as making telephone service widely available throughout the United States at reasonable rates.**

Definition (continued)

SWBT believes that Universal Service is not a particular set of services or a specific type of technology. Universal Service and basic telephone service are not synonymous. Instead, Universal Service is a concept that relies on the deployment of a telecommunications infrastructure or platform (loop, switching, and interoffice facilities, or equivalent) for use by the general public to accomplish two-way switched voice communications within and beyond a local calling area. This basic infrastructure is necessary to provide the access to services and capabilities that exist today. Without this infrastructure, ubiquitous service would not be possible. Using the Universal Service platform, a number of services can be offered to the consumer, including basic telephone service. The Universal Service basic infrastructure has been deployed ubiquitously by the Local Exchange Carriers (LECs) to serve all communities and customers, both high cost and low cost -- rural and urban. Thus, the ultimate definition of Universal Service must recognize this ubiquitous infrastructure and should also be sufficiently broad in order to accommodate changing needs.

There is also much debate concerning whether Universal Service should now include an advanced network in order to take advantage of the services which could be available under the proposed "Information Superhighway". To address a definition of Universal Service that would include an advanced network would also require investigating the costs associated with the deployment of such a network, potential widespread use and customer demand, coupled with an analysis of how such a network would be funded. More discussion of this issue may be found in the "Expanded Definition of Universal Service" section of this paper.

Carrier of Last Resort

Another issue that is receiving much attention involves the carrier of last resort obligations. Historically, state regulators and legislators have established local franchise areas and designated the LEC to serve as the carrier of last resort, including fulfilling readiness to serve and service quality requirements, within their prescribed local franchise area. As the carrier of last resort, LECs were required to serve all customers within their certificated territory. This obligation to serve on an initial and continual basis was balanced with the LECs' right to serve as the exclusive franchised provider.

Carrier of Last Resort (continued)

LECs were required to deploy the necessary facilities and equipment in advance of actual demand in order to be "ready to serve". LECs were also required to maintain certain levels of service quality, adhere to maintenance intervals, and provide accessibility to business office and repair bureaus, among other things. Regulatory rules and policies were also implemented to treat the depreciation of facilities and equipment over an extended period of time, and to develop average prices/costs over large geographic areas. Further, social policy pricing of certain services was used in order to achieve Universal Service objectives. For example, basic residential local service prices were kept low by realizing substantial amounts of cost recovery from other services (i.e., IntraLATA toll, access services, etc.).

These types of rules and regulations were acceptable in an exclusive-provider environment. These rules and regulations, however, are no longer sustainable in a competitive environment. Once competition is introduced into a marketplace, the inevitable result is that alternative providers, which are given regulatory advantages, are able to undercut the LECs' regulated rates and thereby attract the most lucrative customers -- high volume/low cost large customers in urban areas. These customers have traditionally paid averaged rates which contributed toward keeping access rates in low volume/high cost areas and local residential service rates low, thus, universally available. As large customers are either siphoned off the LECs' network, or retained by the LECs through deaveraged competitive prices, residential customers and customers in rural America will inevitably be faced with the possibility of increased prices -- as prices for each service must be more closely aligned with underlying costs.

Thus, if the goal of public policy makers is a competitive marketplace then the regulatory rules and policies implemented in the presence of a monopolistic environment must change to permit fair and equal competition. The level of regulation must be equal for all participants within a competitive area to ensure equal competition, so its full benefits are realized by customers rather than certain providers. **While SWBT will maintain carrier of last resort obligations, it must be allowed a fair opportunity to recover its costs via rate rebalancing and/or interconnection charges and/or implementation of explicit support mechanisms.**

Universal Service Voucher System

Some parties have advanced an idea which they claim will ensure the continuation of Universal Service. This idea known, among other things, as a voucher system or a balloting process, is premised on giving individual customers a "credit" so they may choose the carrier they wish to provide their service. At first glance, such a system could have some appeal since it seems to provide customers with a choice. **SWBT believes that such a system is an inappropriate attempt to selectively obtain support amounts. SWBT believes that such a system will actually jeopardize Universal Service rather than support it (as discussed below).**

Merely giving customers a "choice" is not the full answer to continuation of Universal Service. The continuation of Universal Service into the future is contingent upon the same basis as Universal Service today: a ubiquitous network for provision of services to all geographic areas (low cost, high cost, etc.) at reasonable rates. Implementation of a Voucher System, or similar mechanism, does not ensure these principles will continue to be met.

Some of the problems with a Voucher System, or a similar mechanism, are that it:

- Does not ensure a ubiquitous network will be available.
- Does not ensure that support will offset the high cost to provide Universal Service by individual companies.
- Could jeopardize carrier of last resort obligations by allowing support to flow to other than the carrier of last resort.
- Ignores the fact that implicit support from averaged rates is needed to keep rates lower in certain geographic areas.

Thus, a Voucher System, or a similar mechanism, <u>WILL NOT</u> ensure the continuation of Universal Service.

Support Mechanisms

Yet another complicated issue involves the support mechanisms which are needed to continue the provision of Universal Service. The present economics of local exchange service involve a number of subsidies and support mechanisms intended to achieve social benefits (i.e., basic residential local service prices were kept low by realizing substantial amounts of cost recovery from other services such as IntraLATA toll, access services, etc.). Similarly, support to higher cost areas (largely rural) is provided via rate averaging.

Current support mechanisms can be categorized as:

- Explicit - identifiable, quantifiable and specifically targeted, i.e., Universal Service Fund (USF), Long Term Support (LTS), Carrier Common Line (CCL), etc.

- Implicit - within LEC rates
  - between services
  - within services, between geographic areas

The recovery of the cost of providing the existing level of Universal Service is embedded in a series of existing explicit and implicit support mechanisms. Explicit support mechanisms are those which are identifiable, quantifiable and specifically targeted. Explicit support mechanisms include the USF, FCC and state approved Lifeline/Link-up programs, and LTS. Some of these explicit mechanisms direct support to the telecommunications service provider while others are directed to the consumer. Implicit support mechanisms are when the rates for certain services provide a level of contribution for other services or geographic areas. Implicit support mechanisms include rate averaging (geographic and other), residual rate making, and allocation of the costs of service (basic local loop) to be recovered through other access and toll and non-basic local charges.

These support mechanisms have been instrumental in achieving the levels of service universally available today at reasonable rates. Further, these support mechanisms were established in large part during an era of only gradual technological change and when a limited number of competitive marketplaces existed.

The telecommunications environment is much different today as technological changes are advancing at a rapid rate and competition in the marketplace is also accelerating very rapidly. Thus, the time is right to review the methods currently in place to provide the funds necessary to ensure the continuation of Universal Service.

Quantification of Support

It has been estimated, in the Calvin Monson and Jeffrey Rohlfs (Monson/Rohlfs) study "The $20 Billion Impact of Local Competition in Telecommunications", that approximately $20 Billion annually, or on average over $12 per month per access line in the United States of revenue "contribution" comes from services facing increased competition. This study indicates that the annual amount primarily goes toward reducing rates for other services and little, if any, goes to earnings of telephone companies. This study also indicates that the $20 Billion annual contribution amount is at risk as a result of competition. The study concludes that the impact of competition will be dramatic and as more and more of the $20 Billion contribution is diverted to competitive providers, commensurate adjustments will need to be made to other rates to compensate for the lost financial support (i.e., contribution).

SWBT estimates that approximately $1.9 Billion of implicit support is embedded in its average rates charged for Transport, Local Switching, State Toll, and CCL services. Further, SWBT estimates that it receives approximately $10 Million of explicit support from the USF, Lifeline, and Linkup programs.

Thus, in the face of competition it has become apparent that a change is necessary to ensure the continuation of Universal Service at reasonable rates. It is also necessary that the burden for Universal Service not be borne by a particular segment of the telecommunications industry. Rather, a more appropriate method would be a process whereby all telecommunications providers contribute financial support toward the funding of Universal Service. Service providers who provide universally available telephone service and are obligated to fulfill a carrier of last resort responsibility should not also be required to provide financial support.

Support Recovery

There are many alternatives to the recovery of support associated with Universal Service. The following describes what may be viewed as the two ends of the spectrum for recovery alternatives.

First, one end of the spectrum for the recovery of Universal Service support is:

Support Recovery (continued)

- Continued targeted support to low income individuals and continuation of existing explicit support to high cost companies through mechanisms, such as USF, LTS, etc.;

- Removal of Universal Service support from LEC prices - reduce price for services;

- Implementation of a **large** explicit support mechanism in both the federal and state jurisdiction. Based on the previously discussed study data the amount needed would approximate **$20 Billion** annually.

However, it does not appear feasible to attempt sole recovery of the total amount of support through such a large explicit support mechanism. A Federal/State Joint Board Recommended Decision and FCC Order, released December 23, 1993, limited the growth of the federally mandated USF, to an estimated $725 Million, nationwide.

Second, a more reasonable approach on the other end of the spectrum seems to be:

- **Pricing flexibility**, including contract based pricing, rate rebalancing, rate deaveraging, new rate elements such as network connection charges, End User Common Line Charge (EUCL) increases, etc. The intent of pricing flexibility is to recover the majority of the support for Universal Service in various rates, both usage sensitive and non-usage sensitive, in order to lessen the amount needed in an explicit support mechanism.

- If necessary, a **small** amount of explicit support for Universal Service providers that serve high cost areas to keep rates charged in these areas reasonable. Such amounts should be funded in a non-discriminatory manner.

- Targeted support for low income individuals, based on a needs test and continuation of existing explicit support mechanisms such as USF, LTS, etc.

The above examples are also shown pictorially in Figure 1.

Support Recovery (continued)

SWBT believes the second alternative would limit the amount of funding needed from an explicit support mechanism as it would permit pricing flexibility for LECs to compete with other providers in competitive market areas. This option would permit the lowering of prices in low cost/high volume areas and permit the adjusting of prices in high cost areas to be closer to the cost of providing service. This alternative also permits the continuation of support to low income individuals based on a needs test.

Some further advantages of pricing flexibility are that it: promotes competition and less regulation; allows an individual jurisdiction to move at its own pace in restructuring the recovery of support; and encourages the development and deployment of new technologies.

Expanded Definition of Universal Service

In addition to the question of a current definition for Universal Service there is much discussion within the industry about the National Information Infrastructure (NII), or Superhighways and a nation of information "haves" and "have nots". Discussion of advanced technology offerings has prompted a call for an expansion of the definition of Universal Service to include a network to handle advanced services. Expanding Universal Service to include an advanced network infrastructure, would also require an investigation of the associated costs, potential of widespread use and customer demand, and how such an expanded definition/network could be funded.

Several estimates have been made of the cost to provide such a network. In "An 'Infostructure' For All Americans: Creating Economic Growth in the 21st Century" it is stated (pg. 3) that the Bell companies will invest in a high performance, advanced intelligent network. This network will consist of broadband fiber optic, high speed digital switches, digital compression, and other state-of-the-art technologies that will allow users to access the nation's expanding computer technology. Based on the estimates of investment required and the expenses to maintain the network, this could cost up to $135 Billion annually.

ınition of Universal Service (continued)

.ecommunications Industries Analysis Project presented a paper ⌈November, 1993 NARUC Meeting entitled "Beyond Future Shock: Need for a New Regulatory Response to Technological Change" ıch also provided an estimate of the investment necessary to provide broadband network. Depending on the capabilities of the broadband network and the extent of deployment, the network could cost up to $126 Billion.

If the definition of Universal Service is expanded to encompass an advanced network, it should be constructed only where the market dictates and customers are willing to purchase services at rates that will provide for the recovery of deployed costs.

If federal policy were to dictate the provision of an advanced network infrastructure, then some portion of the investment may need to be recovered through an infrastructure support mechanism.

Related Activity

AT&T USF Petition

On November 24, 1993, AT&T filed a Petition requesting the FCC address the method used to allocate USF costs among Interexchange Carriers (IXCs) (AT&T filed a similar Petition on August 8, 1989). Specifically, AT&T proposes interim procedures which would allocate USF costs among IXCs based upon the IXCs' revenues or minutes, in lieu of the current method based upon presubscribed lines. The FCC released the AT&T Petition for public comment and established RM-8408.

On January 14, 1994, approximately 36 parties filed comments in response to the AT&T Petition. **The majority of commentors generally concur that the method for allocating USF costs needs to be reviewed and should be considered in a comprehensive review of all Universal Service issues**. However, a few parties argued that the existing method of allocating USF costs, based on presubscribed lines should be retained and the AT&T Petition denied on the basis that AT&T has not shown the existing method to be unfair or unlawful.

Related Activity (continued)

NARUC

In response to an MFS Petition for Notice of Inquiry (NOI) (filed on November 1, 1993), NARUC adopted a Resolution addressing Universal Service on November 17, 1993 which:

- supports a comprehensive review of the concept of Universal Service, and issues related to its continuation and expansion;
- requests the FCC to issue an NOI in response to the MFS Petition and review all Universal Service issues; and
- indicates that NARUC endorses use of a collaborative process with the FCC, National Telecommunications and Information Administration (NTIA) and others to address issues related to Universal Service.

NARUC has also begun evaluating many issues surrounding Universal Service. As part of this evaluation, NARUC is drafting a series of papers to address various Universal Service issues. Included are papers addressing cost and funding considerations; technical standards; views on Universal Service; and monitoring and enforcement. SWBT will address the NARUC papers in a separate response at a later date.

MFS

On November 1, 1993, MFS filed a Petition for an NOI and en banc hearing to determine future policies for continuing to promote Universal Service in a competitive environment. MFS' stated objective is to assist the Commission in determining an equitable, non-discriminatory, and competitively neutral funding mechanism that will permit MFS to fulfill its obligation to contribute to the funding of Universal Service as opposed to current mechanisms that according to MFS place a disproportionate burden on competitive entrants.

MFS has suggested four issues that the Commission should investigate:

- Which services or users require subsidization, and should the Commission continue to subsidize "high-cost" rural exchanges?
- How much subsidy is actually required?
- Who should administer subsidy programs?, and
- How should subsidy funds be raised?

Related Activity (continued)

SWBT agrees that the Universal Service issues raised in MFS' Petition warrant Commission attention, but is opposed to the FCC conducting a Universal Service proceeding before issuing a Notice of Proposed Rulemaking (NPRM) in response to the United States Telephone Association (USTA) access charge Petition. The Commission can issue the access charge reform NPRM sought by USTA without any concerns over the potential ill effects upon Universal Service.

Teleport

During December 1993, Teleport released a paper entitled "Universal Service Assurance (USA)". Teleport's proposal underscores the general industry consensus that a comprehensive review of Universal Service issues is critical to facilitate faster growth of competition while assuring continuance of Universal Service.

This paper proposes what Teleport refers to as "equal access to the local exchange subsidies". Teleport reasons that under its plan a competitor in the local exchange market would willingly serve high-cost or low-income consumers, "so long as it could receive for each such customer the same subsidy that the incumbent provider receives." Teleport explains that if the competitors cannot have access to such subsidies "regulators and telephone companies can hardly fault competitors for not serving such customers."

SWBT has conducted an analysis of the Teleport paper and has found several areas of concern. 1) The existing Universal Service subsidies are designed to recover the costs of the existing ubiquitously deployed infrastructure. Teleport appears to suggest that the new subsidies it is proposing would be funded primarily by the very LECs that have built the current ubiquitous infrastructure. This is not practical because it requires the LECs to pay for the costs they already incurred for providing Universal Service. 2) The proposal takes a new way of looking at Universal Service as it suggests that not only should customers have choices, but carriers will also have the choice to serve or not-to-serve a customer or market. 3) The paper raises numerous other questions which will also need to be answered.

For a copy of SWBT's complete analysis of this proposal see the Energy and Regulatory Matters Information Service (ERMIS) Bulletin Board, File #160426, February 11, 1994.

Related Activity (continued)

Eli Noam

Eli Noam, Columbia University, released a paper entitled "NetTrans Accounts", which establishes certain principles for reformed Universal Service. These principles suggest that the new system of Universal Service should: (1) not skew the relative market strength of any carrier; (2) not favor or disfavor integrated or unbundled provision of a service; (3) not favor any type of transmission technology over others; (4) not favor any particular use of telecommunications, or type of message; (5) not burden any parts of the country disproportionately; (6) not result in a shock or windfall to any participants; and (7) be integratable into the federal-state regulatory system.

The paper also suggests that successful revenue raising systems should meet the following criteria: (1) there should be no rate shocks, windfalls, or unilateral advantages to some competitors; (2) should have stability in generating the targeted revenues; (3) must be simple; (4) may not require overturning existing Universal Service system; and (5) should provide incentives to production efficiencies. The paper recommends a complex system of "NetTrans Account" for purposes of payment and receipt of Universal Service support.

SWBT has conducted an analysis of the Noam paper, and found several areas of concern. First, assuming full competition, which is an underlying premise of the proposal, would a NetTrans Account System really be necessary? Second, the paper only addresses Universal Service from the aspect of providing explicit subsidies to end users. Ensuring users' connection to the network at reasonable rates is just one aspect of Universal Service. The existence of a reliable ubiquitous network to serve all areas regardless of the level of efficiency is another. For Universal Service to be a reality, recovery of the network costs which have been incurred by LECs is necessary. Instead, this proposal will impose a double burden on the LECs.

One, LECs will incur costs for facilities and employees necessary for meeting Universal Service requirements; and two, they will have to pay for a portion of their own and other local exchange providers' Universal Service costs. This is unfair since the LECs' competitors are not required to incur facility or operational costs to provide Universal Service. This proposal may require quantification of the aggregate subsidy amount required to maintain Universal Service in the United States. This will certainly be a monumental and costly task since subsidies are not routinely calculated as part of the regulatory process. The proposal requires LECs and others to calculate net transmission path revenues.

Related Activity (continued)

While these are available for LECs' interstate access services (transport and local switching revenues), they are not available for toll services, CAP services, and other services. The paper is also inconsistent with its goal of being "competitively neutral". Finally, NetTrans may not reduce actual subsidy requirements.

For a copy of SWBT's complete analysis of this proposal see the Energy and Regulatory Matters Information Service (ERMIS) Bulletin Board, File #163956, posted March 8, 1994.

MCI

MCI's paper, "From a Single Lane to the Superhighway: Rethinking Universal Service Policy for the 21st Century Consumer" is based on the premise that introduction of competition in the local market will bring choice and lower prices to the local telephone subscribers. Consequently, MCI suggests that a revised Universal Service policy will be needed to facilitate the transition to local competition.

MCI's proposal emphasizes that it is now time for a comprehensive review of Universal Service issues. MCI points out that "while everyone agrees Universal Service should remain a vital component of future telecommunications policy, the combination of new technologies and a changing marketplace have rendered the current system obsolete."

MCI is quick to criticize the level of LEC costs incurred to provide Universal Service even though the paper does not contain any support that shows how their proposal will maintain or improve Universal Service. Irrespective of MCI's unfounded allegations about the impropriety of LEC costs to provide Universal Service, SWBT strongly believes that LECs should have the ability to recover the costs it has and continues to incur to build and maintain a network that provides ubiquitously available Universal Service.

SWBT supports the following basic approach for recovery of Universal Service costs in the competitive marketplace:

- LECs should be allowed rate rebalancing and pricing flexibility;
- If pricing flexibility is limited, other means should be allowed for LECs to recover costs associated with Universal Service from all users of the public switched network;

Related Activity (continued)

- Subsequent to rate rebalancing, additional explicit mechanisms should be targeted to end users who cannot afford basic telephone service; and

- Existing explicit support mechanisms (USF, LTS, Lifeline, Link-up, etc.) should be maintained.

MCI appears to suggest that either the existing network would have to be abandoned or two parallel networks would have to be subsidized. Neither one of these choices results in specific customer benefits. MCI's paper is silent regarding its commitment to provide Universal Service. MCI suggests that LEC cost recovery used to provide for Universal Service is an over-inflated number and really reflects the cost of their inefficient monopoly operations. MCI's allegations merely rely on a worn-out argument that LEC costs exceed "economic costs". SWBT agrees with MCI that Universal Service should be funded on an "equitable and competitively neutral basis". The MCI proposal is, however, far from being equitable and competitively neutral.

For a copy of SWBT's complete analysis of this proposal see the Energy and Regulatory Matters Information Service (ERMIS) Bulletin Board, File #167622, posted April 5, 1994.

Clinton Administration

On January 27, 1994, the Clinton Administration released a White Paper on telecommunications policy. The paper expands on Vice President Al Gore's speech at the "Superhighway Summit", which outlined the Administration's proposals to reform the communications marketplace through development of a National Information Infrastructure (NII) and telecommunications legislation.

The Administration supports removal of the legislative, judicial, and regulatory restrictions which now apply to the telecommunications, cable TV, and information industries, because they are limiting economic growth. Legislation to be introduced, should incorporate the following five principles:

1) Encourage private investment in the NII;

2) Promote and protect competition;

Related Activity (continued)

3) Promote open access to the network to all information providers and consumers;

4) Avoid the creation of telecommunications/technology "haves" and "have nots" through development of a new definition of Universal Service;

5) Encourage flexible telecommunications policies, permitting policy makers to adapt to change.

The paper discusses the specifics for legislation regarding Local Competition and Interconnection; Relations With the States; Regulatory Flexibility; Regulation of Two-Way Broadband Transmission Services; Cable-Telephone Crossownership; and Universal Service. In the discussion regarding Universal Service issues, the Administration states a desire "to develop an enhanced concept of Universal Service that will serve the information needs of the American people in the 21st century". Briefly, its proposals to do so include:

- A goal that by the year 2000, all classrooms, libraries, hospitals, and clinics will be connected to the NII. Proposed is an annual nation-wide survey of the availability of advanced telecommunications services to such locations, as well as possible tariffing of preferential rates for interstate services to ensure that standards are in place to permit uniform interconnection to the NII.

- An offer for guidance and flexibility to the FCC and states in specifying objectives for Universal Service. For instance, the Administration suggests that "advanced services should be available to rural and urban lower income users, to users in areas where the costs of service are high, and to social institutions, especially educational and health-care facilities".

- Charging the FCC and the states with responsibility for reviewing the objectives for expanding Universal Service to meet changing circumstances.

- Support of the requirement of H.R. 3636 (discussed below) that the FCC and the states address Universal Service issues through a Federal/State Joint Board.

Related Activity (continued)

- Support for the FCC and the states to have "broad authority" regarding establishment of requirements of service providers to contribute to the preservation of Universal Service. They must, however, "ensure that no service provider is unfairly burdened relative to its rivals" or that contributions "do not unduly distort consumer choices".

- A proposal for the authorization of "sliding scale" or "in-kind" contributions in lieu of cash payments, (not provided for in H.R. 3636).

The Administration supports the general approach of H.R. 3636 and the provisions thereof. Therefore, it has decided not to introduce free-standing legislation regarding reform of telecommunications policy.

Legislation

There are currently two major pieces of legislation that address and make specific provisions for Universal Service regulation. They are H.R. 3636--National Communications And Information Infrastructure Act of 1993 and S.1822--Communications Act of 1994. Another piece of legislation, House bill H.R. 3626--The Antitrust Reform Act of 1993, addresses the restrictions of the Modified Final Judgement (MFJ) and is not specifically concerned with Universal Service, but could potentially impact Universal Service issues as MFJ restrictions are removed.

H.R. 3636

This bill is divided into two sections: Infrastructure and Competition; and, Communications Competitiveness. Universal Service related components of this bill are that it:

- Requires that a Joint Board be convened to make recommendations on the preservation and definition of Universal Service and support mechanisms;

- Provides guidelines for the Joint Board to follow:

  - to ensure continued viability at affordable prices;
  - to define carrier obligations:
  - to include advanced services in the definition of Universal Service;
  - to establish support mechanisms to which all providers of telecommunications must contribute;

Related Activity (continued)

- Holds the FCC ultimately responsible for the timely implementation of Universal Service regulation.

S.1822

This bill contains provisions that complement H.R. 3636; it addresses infrastructure, regulatory flexibility, and Universal Service. Specifically, on Universal Service regulation it:

- Requires every common carrier to contribute to Universal Service;

- Holds the FCC responsible for providing guidelines for the Universal Service definition, though allows it to delegate primary responsibility for defining Universal Service and ensuring goals are met to the states;

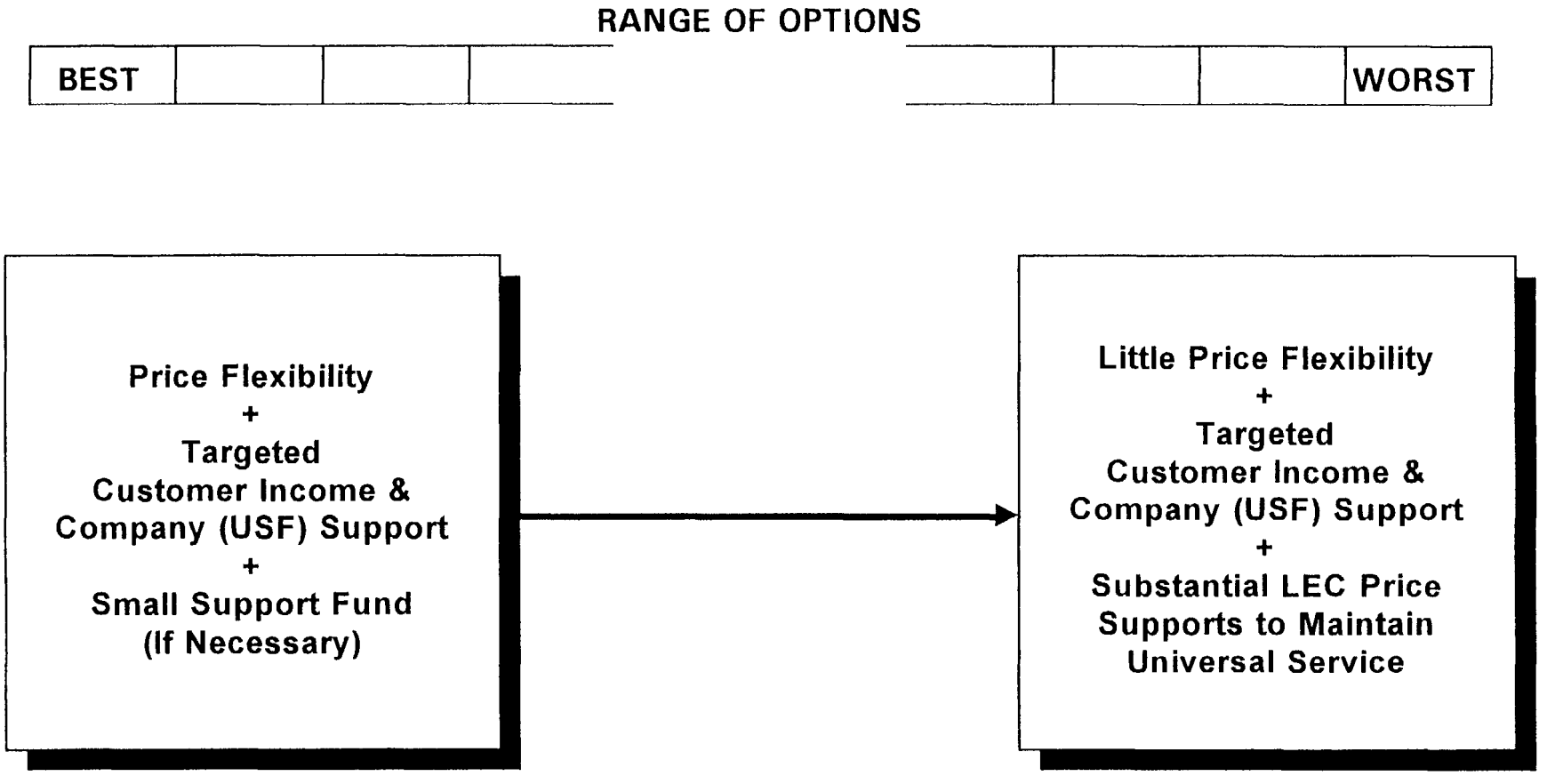
- Requires the FCC to ensure that interstate telecommunications providers contribute to a fund for the preservation of Universal Service on a competitively neutral basis, to be distributed to each state;

- Allows the states some flexibility regarding distribution of assistance from the fund to support protecting and advancing Universal Service;

The effect of all of these bills, still pending in Congress, is to move regulation from the courts to Congress.

Figure 1

OPTIONS FOR FUNDING PROVISION/MAINTENANCE OF UNIVERSAL SERVICE



1) What steps are required to protect Universal Service in a competitive marketplace, i.e.:

- Is *rate rebalancing required?*

  Competition will make rate rebalancing necessary. Average rates cannot be maintained in competitive areas. Competitors will enter low cost/high volume markets where contribution is currently being generated to support rural operations as well as other higher cost operations. LECs will have no choice but to raise local, toll and access rural rates if they plan to sustain their current revenue levels. An alternative to raising rural or local exchange rates would be to maintain the current transport residual interconnection charge and expand it to include other support such as CCL. In any case, the current revenue levels are necessary to support the ubiquitous network which satisfies current universal service objectives.

- **Should rural areas be treated differently?**

  Rate rebalancing will likely produce rates that are higher in rural areas that are higher cost. If these rebalanced rates are unaffordable to low income rural customers, then support can be targeted to these customers. Finally, if a rate differential is viewed as a significant disadvantage to rural America, an average interconnection charge, such as the transport RIC, targeted to LECs serving these areas should be implemented.

  See Tab 5C of this binder for more information related to this subject.

2) What services are included in Universal Service - and at what price to customers?

- **The range of options stretch from what is being provided today to the REA proposed requirements.**

  First, current Universal Service should not be defined in terms of a particular set of services or technology. Universal Service should be defined as the basic network infrastructure or platform (loop, switching and interoffice facilities) needed to complete two-way switched voice communications within and beyond a local calling area. The LECs have deployed this universally available ubiquitous network. Using this Universal Service platform, a number of services can be offered to the consumer, including basic telephone service. However, basic telephone service is not synonymous with Universal Service, rather it is a service that is available because the Universal Service infrastructure has been deployed. Without the infrastructure, no services could be offered. Support for that infrastructure, through implicit (rate averaging and CCL, etc.) or explicit (USF, etc.) mechanisms must be continued in order to provide Universal Service. Support to maintain affordable basic service rates for targeted groups of customers may also be required (i.e., Lifeline, Linkup, etc.).

Universal basic telephone service as defined by SWBT in its response to the NARUC Universal Service Questionnaire dated November 1, 1993, could include:

- Two way voice grade access to the public switched network
- Access to local emergency services
- Standard intercept service
- Standard directory listing
- Facilities designed for voice communications
- Equal access to interexchange carriers

The network being proposed by the REA would significantly expand the definition of the Universal Service infrastructure. With an expanded network infrastructure, as proposed by the REA, consumers would likely have access to more advanced services. However, this expanded network does not come without cost (the SBC/SWBT response to the REA proposal estimates it would take SWBT at least $25B in investment to meet the REA proposal; the nationwide amount has been estimated to range from $230B - $420B depending on the level of deployment or, conservatively, $50 per customer loop per month). An expansion of the current network to include broadband services should only occur as the market dictates (where customers are willing to pay).

The LECs must be permitted to recover the costs they have already incurred to build the network required to fulfill Universal Service obligations. A carrier should be given the regulatory flexibility to rebalance and deaverage rates in order to be competitive and to recover the costs to provide Universal Service. If pricing flexibility is limited, then the Universal Service provider should be permitted to recover the remainder of its support costs from an explicit support mechanism. If, after this process is completed, there are still certain end users who cannot afford telephone service, then these end users should have assistance available to them, based on a financial needs test, in the form of a credit on their monthly bill.

See Tab 4 of this binder for more information related to this subject.

3) How should the USF be modified, i.e.:

- **Reduce the maximum expense adjustment from 75% to 65%? NO**
- **Eliminate overheads from the USF formula? NO**
- **Reduce USF payments, if local service rates are below threshold? NO**
- **Consolidate multiple study areas under common control for USF purposes? NO**
- **Eliminate USF payments to ECs whose USF payments are less than one dollar per month? NO**
- **Other? Possibly Remove Large LECs from the Fund**
- **None of the above?**